

POTLATCH CORP
Form 10-K
February 13, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 10-K

(Mark One) ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2014
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the transition period from _____ to _____.

Commission File Number 1-32729
POTLATCH CORPORATION
(Exact name of registrant as specified in its charter)

Delaware 82-0156045
(State or other jurisdiction of incorporation or (IRS Employer Identification No.)
organization)
601 West 1st Ave., Suite 1600
Spokane, Washington 99201
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code: (509) 835-1500
Securities registered pursuant to Section 12(b) of the Act:

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
Common Stock (\$1 par value)	The Nasdaq Global Select Market

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

The aggregate market value of the common stock held by non-affiliates of the registrant at June 30, 2014, was approximately \$1,680.5 million, based on the closing price of \$41.40.

As of January 31, 2015, 40,605,179 shares of the registrant's common stock, par value \$1 per share, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for the 2014 annual meeting of stockholders expected to be filed with the Commission on or about April 1, 2015 are incorporated by reference in Part III hereof.

POTLATCH CORPORATION AND CONSOLIDATED SUBSIDIARIES

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EXPLANATORY NOTE

For purposes of this report, any references to "the company," "us," "we," and "our" include Potlatch Corporation and its consolidated subsidiaries.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This report contains, in addition to historical information, certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including without limitation, statements regarding:

- timber inventory;
- payments under timber cutting contracts;
- increasing lumber demand and pricing in North America in 2015;
- increased North American housing starts and repair and remodel activity;
- the expected positive effect on timber prices of increased lumber demand and higher lumber prices;
- expected sawlog prices in 2015;
- expected increase in 2015 timber harvest volume of 800,000 tons from acquisition of Alabama and Mississippi timberlands;
- expected generation of \$1.5 million in annual revenues from recreational leases in Alabama and Mississippi;
- expected harvest level of between 4.0 million and 4.8 million tons each year over the next 15 years;
- expected 2015 overall timber harvest of 4.5 million tons;
- expected sale of 37% of Northern region timber volume under log supply agreements in 2015;
- expected volumes and value of timber to be sold in the Southern region in 2015 under log supply agreements;
- expected sales of 80,000 acres of higher and better use (HBU) property, 140,000 acres of rural real estate property and 80,000 acres of non-strategic timberland over the next decade or more;
- funding of our dividend distributions in 2015;
- compliance with REIT tax rules;
- FSC® and SFI® certification of our timberlands;
- expectations regarding premium prices for FSC®-certified logs and FSC®-certified lumber;
- realization of deferred tax assets;
- expected capital expenditures in 2015;
- expectations regarding funding of our pension plans in 2015;
- expectations regarding supplemental pension plan payments in 2015:
- estimated future benefit payments;
- estimated future payments under operating leases;
- estimated future debt payments; and
- expected liquidity in 2015 to fund our operations, regular stockholder distributions, capital expenditures and debt service obligations and related matters.

Words such as "anticipate," "expect," "will," "intend," "plan," "target," "project," "believe," "seek," "schedule," "estimate," "and similar expressions are intended to identify such forward-looking statements. These forward-looking statements reflect our current views regarding future events based on estimates and assumptions, and are therefore subject to known and unknown risks and uncertainties and are not guarantees of future performance.

Our actual results of operations could differ materially from our historical results or those expressed or implied by forward-looking statements contained in this report. Important factors that could cause or contribute to such differences include, but are not limited to, the following:

- changes in timber growth rates;
- changes in silviculture;
- timber cruising variables;
- changes in state forest acts or best management practices;
- changes in timber harvest levels on our lands;
- changes in timber prices;
- changes in timberland values;
- changes in policy regarding governmental timber sales;

- changes in the United States and international economies;
- changes in interest rates and discount rates;

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- changes in requirements for FSC® or SFI® certification;
- changes in the level of residential and commercial construction and remodeling activity;
- changes in tariffs, quotas and trade agreements involving wood products;
- changes in demand for our products;
- changes in production and production capacity in the forest products industry;
- competitive pricing pressures for our products;
- unanticipated manufacturing disruptions;
- changes in general and industry-specific environmental laws and regulations;
- unforeseen environmental liabilities or expenditures;
- weather conditions;
- changes in raw material and other costs;
- collectability of amounts owed by customers;
- changes in federal and state tax laws;
- the ability to satisfy complex rules in order to remain qualified as a REIT; and
- changes in tax laws that could reduce the benefits associated with REIT status.

For a discussion of some of the factors that may affect our business, results and prospects, see Part 1 - Item 1A. Risk Factors.

Forward-looking statements contained in this report present our views only as of the date of this report. Except as required under applicable law, we do not intend to issue updates concerning any future revisions of our views to reflect events or circumstances occurring after the date of this report.

Part I

ITEM 1. BUSINESS

General

Potlatch Corporation is a real estate investment trust (REIT) that owns approximately 1.6 million acres of timberlands in Alabama, Arkansas, Idaho, Minnesota and Mississippi. We derive much of our income from investments in real estate, including the sale of standing timber. Through wholly owned taxable REIT subsidiaries, which we refer to collectively in this report as Potlatch TRS, we operate a real estate sales and development business and five wood products manufacturing facilities that produce lumber and plywood.

Our businesses are organized into three operating segments:

Resource: Our Resource segment manages our timberlands to optimize revenue producing opportunities while adhering to our strict stewardship standards. Management activities include planting and harvesting trees and building and maintaining roads. The Resource segment also generates revenues from activities such as hunting leases, recreation permits and leases, mineral rights leases, biomass production and carbon sequestration.

Wood Products: Our Wood Products segment manufactures and markets lumber and plywood.

Real Estate: The business of our Real Estate segment consists primarily of the sale of land holdings deemed non-strategic or identified as having higher and better use alternatives. The Real Estate segment engages in real estate sales, subdivision and development activities through Potlatch TRS.

Additional information regarding each of our operating segments is included in this section, as well as in Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 16: Segment Information in the Notes to Consolidated Financial Statements.

We are focused on the ownership of timberland, which we view as a unique and attractive asset due to the renewable nature of timber resources and timber's long-term history of price appreciation in excess of inflation. Our primary objectives include using our timberland investments to generate income and maximizing the long-term value of our assets. We pursue these objectives by adhering to the following strategies:

Managing our timberlands to improve their long-term sustainable yield. We manage our timberlands in a manner designed to optimize the balance among timber growth, prudent environmental management and current cash flow, in order to achieve increasing levels of sustainable yield over the long term. We may choose to harvest timber at levels above or below our then-current estimate of sustainability for short periods of time, including improving the long-term productivity of certain timber stands or in response to market conditions. In addition, we focus on optimizing timber returns by continually improving productivity and yields through advanced silvicultural practices that take into account soil, climate and biological considerations.

Pursuing attractive acquisitions. We actively pursue timberland acquisitions that meet our financial and strategic criteria. The critical elements of our acquisition strategy generally include acquiring properties that complement our existing land base, are immediately cash flow accretive and have attractive timber or higher and better use (HBU) values.

Maximizing the value of our non-core timberland real estate. A portion of our acreage is more valuable for development or recreational purposes than for growing timber. We continually assess the potential uses of our lands and manage them proactively for the highest value. We have identified approximately 20% of our timberlands as having values that are potentially greater than timberland values.

Practicing sound environmental stewardship. We pursue a program of environmental stewardship and active involvement in federal, state and local policymaking to maximize our assets' long-term value. We manage our timberlands in a manner consistent with the principles set forth by the Sustainable Forestry Initiative® (SFI®) or Forest Stewardship Council® (FSC®).

Potlatch Corporation, formerly known as Potlatch Holdings, Inc., was incorporated in Delaware in September 2005 to facilitate a restructuring to qualify for treatment as a REIT for federal income tax purposes. It is the successor to the business of the original Potlatch Corporation, which was incorporated in Maine in 1903.

Effective January 1, 2006, we restructured our operations to qualify for treatment as a REIT for federal income tax purposes. As a REIT, if we meet certain requirements we generally are not subject to federal and state corporate income taxes on our income from investments in real estate that we distribute to our stockholders, including the income derived from the sale of standing timber. We are, with some exceptions, subject to corporate taxes on certain built-in gains (the excess of fair market value over tax basis at January 1, 2006) on sales of real property (other than timber) held by the REIT through December 31, 2015. We are required to pay federal corporate income taxes on income from our non-real estate investments, principally the operations of Potlatch TRS.

Available Information

We make available on or through our website, www.potlatchcorp.com (under “Investor Resources – Financial Information”), our periodic and current reports that we file with, or furnish to, the Securities and Exchange Commission (SEC), at no charge as soon as reasonably practicable after we electronically file the information with, or furnish it to, the SEC. Information on our website is not part of this report. In addition, the reports and materials that we file with the SEC are available at the SEC’s website (<http://www.sec.gov>) and at the SEC’s Public Reference Room at 100 F Street N.E., Washington DC 20549. Interested parties may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

Business Segments

Resource Segment

Industry Background. The demand for timber depends primarily upon the markets for wood related products, including lumber, panel products, paper and other pulp-based products. The end uses for timber vary widely, depending on species, size and quality. Historically, timber demand has experienced cyclical fluctuations, although sometimes at different times and rates for products or geographic regions. The demand for sawlogs, lumber and other manufactured wood products is significantly dependent upon the level of new residential construction and remodeling activity, which, in turn, is affected by general economic and demographic factors, including population growth, new household formations, interest rates for home mortgages and construction loans, and credit availability. Increases in residential construction and remodeling activities are generally followed by higher lumber prices, which are usually followed by higher log prices. The demand for pulpwood is dependent on the paper and pulp-based manufacturing industries, which are affected by domestic and international economic conditions, global population growth and other demographic factors, industry capacity and the value of the U.S. dollar in relation to foreign currencies. Locally, timber demand also fluctuates due to the expansion or closure of individual wood products and pulp-based manufacturing facilities.

The supply of timber has been significantly affected by reductions in timber sales by the United States government and by state governments, particularly in the western United States. These reductions have been caused primarily by increasingly stringent environmental and endangered species laws and by a change in the emphasis of domestic governmental policy toward habitat preservation, conservation and recreation, and away from timber management. Because most timberlands in the southeastern United States are privately owned, changes in sales of publicly owned timber affect local timber supplies and prices in the Southeast less immediately than in the western United States with a much larger proportion of public timber ownership. Timber supplies can fluctuate depending upon factors such as changes in weather conditions and harvest strategies, as well as occasionally high timber salvage efforts due to storm damage, unusual pest infestations such as the mountain pine beetle, or fires. Local timber supplies also change in response to prevailing timber prices. Rising timber prices often lead to increased harvesting on private timberlands, including lands not previously made available for commercial timber operations. The supply of timber generally is adequate to meet demand, although this could tighten as a result of higher U.S. housing starts, the effect of the mountain pine beetle infestation in western Canada, the level of log and lumber exports to Asia from the U.S. and Canada, and the level of annual allowable cut in Canada.

Timberland Acquisition. On December 7, 2014, we acquired approximately 201,000 acres of timberland in Alabama and Mississippi for \$384 million. The acquisition complements our existing ownership in our Southern Region. The acquired timber consists of approximately 73% softwood and 27% hardwoods, and is expected to increase annual timber harvest volumes by approximately 800,000 tons in 2015. We bought the timberland subject to three supply agreements. In addition, we assumed recreational leases that cover approximately 90% of the timberlands acquired.

They are generally annual leases that are subject to renewal and are expected to generate approximately \$1.5 million in annual revenues.

Ownership. The Resource segment manages approximately 1.6 million acres of timberlands in the North, consisting of our Idaho and Minnesota timberlands, and the South, consisting of our Alabama, Arkansas and

Mississippi timberlands. This total includes approximately 17,000 acres under long-term leases. We are the largest private landowner in Idaho. The following table provides additional information about our timberlands.

REGION	STATE	DESCRIPTION	ACRES (thousands)
Northern region	Idaho	Variety of commercially viable softwood species, such as grand fir, Douglas fir, inland red cedar and other associated softwoods	791
	Minnesota	Primarily aspen, pine and other mixed hardwoods	178
		Total Northern region	969
Southern region	Alabama	Primarily southern yellow pine and other hardwoods	101
	Arkansas	Primarily southern yellow pine and other hardwoods	410
	Mississippi	Primarily southern yellow pine and other hardwoods	100
		Total Southern region	611
		Total	1,580

Operation. The primary business of the Resource segment is the management of our timberlands to optimize the value of all possible revenue producing opportunities while adhering to our strict stewardship standards. Management activities include planting and harvesting trees and building and maintaining roads. The segment also generates revenues from non-timber resources such as from hunting leases, recreation permits and leases, mineral rights leases, biomass production and carbon sequestration.

We strive to maximize cash flow while managing our timberlands sustainably over the long term. From time to time, we may choose, within the parameters of our environmental commitments, to harvest timber at levels above or below our estimate of sustainability for short periods in order to take advantage of strong demand or to adjust to weak demand. To maximize our timberlands' long-term value, we manage them intensively, based upon timber species and local growing conditions. Our harvest plans take into account changing market conditions, are designed to contribute to the growth of the remaining timber, and reflect our policy of environmental stewardship. We reforest our acreage in a timely fashion to enhance its long-term value. We employ silvicultural techniques to improve timber growth rates, including vegetation control, fertilization and thinning. In deciding whether to implement any silvicultural practice, we analyze the associated costs and long-term benefits, with the goal of achieving an attractive return over time.

Inventory. As of the end of 2014, our estimated standing merchantable timber inventory was 68 million tons, including 37 million tons in the North and 31 million tons in the South. This estimate is derived using methods consistent with industry practice and is based on statistical methods and field sampling. The estimated inventory volume includes timber in environmentally sensitive areas where the timberlands are managed in a manner consistent with best management practices, state forest practice acts and the SFI® or FSC® forest management standards. The aggregate estimated volume of current standing merchantable timber inventory is updated annually to reflect increases due to reclassification of young growth to merchantable timber when the young growth meets defined diameter specifications, the annual growth rates of merchantable timber and the acquisition of additional merchantable timber, and to reflect decreases due to timber harvests and land sales. Timber volumes are estimated from cruises of the timber tracts, which are generally completed on a five to ten year cycle. Since the individual cruises collect field data at different times for specific sites, the growth model projects standing inventory from the cruise date to a common reporting date. Annual growth rates for the merchantable inventory have historically been in the range of 2%-5% in the North and 6%-9% in the South.

Harvest. Our short-term and long-term harvest plans are critical factors in our long-term management process. Each year, we prepare a harvest plan designating the timber tracts and volumes to be harvested during that particular year. Each harvest plan reflects our analysis of the age, size and species distribution of our timber, as well as our expectations about harvest methods, growth rates, the volume of each species to be harvested, anticipated acquisitions and dispositions, thinning operations, regulatory constraints and other relevant information. Among other things, the optimal harvest cycles, or rotations, for timber vary by location and species and tend to change over time as a result of silvicultural advances, changes in the markets for different sizes and ages of timber and other factors. Since harvest plans are based on projections of weather, timber growth rates, regulatory constraints and other assumptions, many of which are beyond our control, there can be no assurance that we will be able to harvest the volumes projected or the

specific timber stands designated in our harvest plans.

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Detailed harvest information by region and product is presented in Management's Discussion and Analysis of Financial Condition and Results of Operations. The following table presents a summary of our total 2014 timber harvest by region.

(in thousands)	TIMBER HARVESTED (TONS)			TOTAL
	SAWLOGS	PULPWOOD	STUMPAGE	
Northern region	1,982	202	16	2,200
Southern region	620	817	22	1,459
Total	2,602	1,019	38	3,659

We expect our harvest level to range between 4.0 million and 4.8 million tons each year over the next 15 years, depending on market conditions and other factors. Based on our current projections that take into consideration such factors as market conditions, the ages of our timber stands and recent timberland sales and acquisitions, we expect to harvest approximately 4.5 million tons in 2015.

The Resource segment sells a portion of its logs at market prices to our wood products manufacturing facilities. Intersegment sales to our wood products manufacturing facilities in 2014 were approximately 25% of our total Resource segment revenues. The segment also sells sawlogs and pulpwood to a variety of forest products companies located near our timberlands. Idaho Forest Group, LLC represented slightly more than 10% of our consolidated revenues in 2014, 2013 and 2012. The segment's customers range in size from small operators to multinational corporations. The segment competes with owners of timberlands that operate in areas near our timberlands, ranging from private owners of small tracts of land to some of the largest timberland companies in the United States. The segment competes pri